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IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1967.

No. 738

JOSEPH W. HART, LUELLA F. HART and J. CARL RUSSELL,
Petitioners,

vs.

FEDERAL RESERVE BANK OF ATLANTA,
Respondent.

PETITION FOR A WRIT OF CERTIORARI

To the United States Court of Appeals for the Sixth Circuit.

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FEDERAL RESERVE BANK OF ATLANTA,
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PETITION FOR A WRIT OF CERTIORARI

To the United States Court of Appeals for the Sixth Circuit.

Petitioners, Joseph W. Hart, Luella F. Hart and J. Carl Russell, ask that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Sixth Circuit rendered in this case on June 21, 1967, which affirmed a judgment of the United States District Court for the Middle District of Tennessee. The opinions below have not been reported but are appended hereto.

GROUND ON WHICH JURISDICTION OF COURT IS INVOKED.

(i) The judgment of the Court of Appeals sought to be reviewed was entered June 21, 1967. Petitioners filed a timely petition to rehear which was denied on July 20, 1967.

(ii) The statutory provision believed to confer on this Court jurisdiction to review the judgment in question by writ of certiorari is 28 U. S. C. 1254 (1).

QUESTIONS PRESENTED.

1. Where a federal reserve bank, purporting to act as fiscal agent of the United States on behalf of the War Department pursuant to Executive Order No. 9112 of March 26, 1942 authorizing the guarantee to commercial banks against loss on loans made to concerns to finance the performance of war orders, executed a guarantee agreement to banks of the balance of loan for defense housing remaining after the 90% portion which was F. H. A. insured, dealt with the collateral in the form of mortgage on the housing development in such manner as, according to applicable state law, amounted to a violation of the fiduciary duty of a pledgee or mortgagee, is it protected by the doctrine of sovereign immunity from liability to the pledgor's guarantors who have suffered injury from a failure to realize the reasonable value of the security for the loan?

2. Is there a privy relationship between the Federal Reserve Bank of Atlanta and the United States which entitles it to invoke the doctrine of collateral estoppel by judgment arising from a finding in a former suit brought by the United States of America against petitioners that they did not carry the burden of substantially proving the defense of breach of duty by the federal reserve bank's assignors, two Alabama banks, in same transaction; and

was the adjudication of the issues raised in the former litigation conclusive of the issues raised in the present case?

3. Is it a misuse of his official power for the Attorney General of the United States to defend this action for the federal reserve bank and to refuse production of the government files which would shed light on the transaction?

STATUTES AND EXECUTIVE ORDERS INVOLVED.

First War Powers Act, 1941—Public Law—Ch. 593—Public Law 354—77th Congress, 1st Sess., Approved December 18, 1941—55 Stat. 838.

Executive Order No. 9070, of February 24, 1942, Consolidating the Housing Agencies and Functions of the Government into the National Housing Agency.

Executive Order No. 9112, of March 26, 1942, Authorizing Financing Contracts to Facilitate the Prosecution of the War.

National Housing Act Amendment—Ch. 319, Public Law 559—77th Congress, 1st Sess., Approved May 26, 1942—56 Stat. 301.

Mobilization of Small Business Act—Ch. 404, Public Law 603, 77th Congress, 1st Sess., Approved June 11, 1942—56 Stat. 351.

The pertinent text or excerpts from the statutes and executive orders involved are set forth in the Appendix hereto.

STATEMENT OF THE CASE.

In 1942 and 1943, The First National Bank of Birmingham, Birmingham, Alabama, and The Merchant's National Bank of Mobile, Mobile, Alabama, loaned an Alabama corporation, Country Club Village Corporation, $2,200,000.00 for the construction of a residential subdivision in Mobile, Alabama. Notes for this amount executed by the corporation were guaranteed by petitioners Hart and Russell individually, they being the owners of all but one share of the capital stock of the corporation. Luella F. Hart, wife of Joseph W. Hart, was the owner of the remaining one share. All of the stock was pledged to secure the obligation of the guarantors.

The loan was further secured by a mortgage executed by the borrowing corporation covering the entire housing development.

The lending banks applied to Federal Reserve Bank of Atlanta, as fiscal agent of the United States, for a guarantee of the loan, pursuant to Executive Order No. 9112 of March 26, 1942. Pursuant to the application, Federal Reserve Bank of Atlanta in the name and on behalf of War Department of the United States and as Fiscal Agent of the United States executed a Guarantee Agreement containing the obligation to purchase, on demand of the banks, 90% of the unpaid principal amount of the loan.

The permanent financing of the subdivision development was to be by F. H. A. guaranteed mortgages on the 425 individual dwelling units after completion. After the completion of the construction and the permanent financing with mortgages guaranteed by F. H. A. for 90% of the replacement cost of the property, a balance of the construction loans made by the two banks in the sum of $183,345.55 remained unpaid. Upon demand of the banks,

the War Department, through Federal Reserve Bank of Atlanta, performed the obligation of the Guarantee Agreement, paying to the two banks $165,742.34.*

Thereafter, the banks controlling the mortgaging corporation through the stock pledge, with the participation of Federal Reserve Bank of Atlanta, made a sale of the entire subdivision to another corporation, Spring Hill Homes, Inc., for $37,170.00.

The note of Country Club Village Corporation and the guaranty signed by Hart and Russell secured by the stock of the corporation were assigned by the banks to Federal Reserve Bank of Atlanta which in turn assigned the same to the United States of America.

In order to effect the sale of the properties, Federal Reserve Bank of Atlanta, purporting to act as Fiscal Agent of the United States of America, released the mortgagor's subsidiary corporation which held the legal title to the subdivision from the obligation to execute a blanket second mortgage upon the subdivision inferior to the F. H. A. guaranteed mortgages on the individual housing units. If this release had not been made, within a few months time, piecemeal sales of the houses would have produced enough to pay in full the indebtedness, which after the assignment was held and owned 10% by the two banks and 90% by the United States of America. The buyer realized a profit of approximately $375,000.00 from the purchase of the subdivision for $37,170.00.

On Nov. 6, 1956 (eleven years after the sale of the subdivision) the United States of America brought suit against

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* In order to hold that such a guaranty was valid, we must assume that Congress, after limiting the authority of the Federal Housing Administrator to insuring 90% loans, proceeded to authorize the War Department to guarantee the payment of the 10% uninsured portion of the loan. (The guarantee here was 90% of the uninsured 10%.) A mere statement of the proposition imputes a near imbecility to Congress.

Hart and Russell on their guaranty of the note for $2,200,000.00 and recovered a judgment against them in the United States District Court for the Middle District of Tennessee on January 29, 1962 for the principal balance remaining due after crediting thereupon the proceeds of the sale and certain other recoveries. The amount of the judgment was $83,900.63 plus interest totaling $119,850.56. This judgment was affirmed on appeal by the Circuit Court of Appeals for the Sixth Circuit. **United States of America v. Joseph W. Hart and J. Carl Russell, 312 F. 2d 127.**

Petitioners on Nov. 6, 1962 sued Federal Reserve Bank of Atlanta in the United States District Court for the Middle District of Tennessee to recover damages for the injury sustained by them from the wanton sacrifice of the security for the indebtedness on which the judgment against Hart and Russell was rendered.

The jurisdiction of the district court was on the ground of diversity of citizenship between plaintiffs-appellants and the defendant Federal Reserve Bank.

The defendant Federal Reserve Bank filed an answer to the complaint which was signed by the United States Attorney. In this answer, while there was no denial of the allegation in the complaint that it participated in making the sale of the assets and property held by the pledgee banks (The First National Bank of Birmingham and the Merchants National Bank of Mobile), it "categorically denied that the sale of the Country Club Subdivision resulted in a wanton sacrifice of the security and that the sale was made in bad faith and was fraudulently contrived. It denied "that there was ever any repudiation of trust or any abuse of trust, and alleges that defendant acted in the capacity of a holder in due course of negotiable papers rather than in a trust capacity."

The defendant's answer, by the United States Attorney, averred as an affirmative defense:

> "19. That the defendant in all its dealings with the plaintiffs, was acting as fiscal agent of the United States and is immune from liability for any act it may have done, both by common law and under the provisions of said Executive Order 9112 (7 Federal Register 2637), which provides in part that 'no Federal Reserve Bank shall have any responsibility or accountability except as agent of the War Department, Navy Department, or Maritime Commission, as the case may be.' "

Plaintiffs, after the filing of the answer, propounded interrogatories to the defendant seeking discovery of "all reports, communications, memoranda, letters, appraisals, documents and other writings in any way pertaining to the sale of the Country Club Village property to Spring Hill Homes, Inc., or L. B. Ellinor" (App. 21a). The defendant obtained an order staying the answering of the interrogatories until thirty days after the court shall have ruled on the validity of the affirmative defenses raised by the defendant in its answer.

Then the defendant by the U. S. Attorney filed a motion for a summary judgment asserting as grounds: *res judicata* by reason of the prior judgment in favor of the United States, governmental immunity from suit and that the action was barred by laches and the statutes of limitations.

Plaintiffs, in their original complaint, made no issue as to lack of authority of the defendant Federal Reserve Bank to act in the transaction as the fiscal agent of the United States of America.

Subsequent to the filing of the motion for a summary judgment, plaintiffs amended par. 9 of their complaint so as to allege lack of authority of the Federal Reserve

Bank to execute the release. As amended par. 9 of the complaint read:

> "9. On or about December 22, 1945, the defendant, purporting to act as fiscal agent of the United States, but without authority in law so to do and for a grossly inadequate consideration executed an agreement reciting that in pursuance to an agreement made prior to the sale of the subdivision property, it had released and discharged the realty from the lien or encumbrance of the agreement dated January 16, 1945, by which the Realty Corporation agreed and bound itself to execute in favor of the defendant, on demand, as security for the balance of the indebtedness of the Village Corporation, a mortgage covering the subdivision subject only to the F. H. A. insured mortgages outstanding on the individual dwelling units thereon."

The Decision of the District Court.

The district court sustained the motion of the defendant for a summary judgment. In its Memorandum opinion, the court directed the entry of an order reciting that the disposition of the motion was based upon the pleadings and exhibits in this action and upon the entire record in the prior case of **United States v. Joseph W. Hart and J. Carl Russell.**

In the Memorandum, the court stated that while the claims and causes of action in this action and the prior action are different, the doctrine of collateral estoppel precluded relitigation between the same parties of issues which were actually litigated and determined in a prior action. Analyzing the complaint in this action, the court, among other things, said:

> "It is clear that the question as to whether the property was sold at a sacrifice was actually litigated

adversely to the plaintiffs in the prior litigation. It was specifically found both by this Court and the Court of Appeals that the price, $37,140.00 was fair and adequate and that the sale was made in good faith. Consequently, this issue cannot be re-examined in the present case as the basis for a claim by the plaintiffs against the Federal Reserve Bank, acting merely in the capacity of a fiscal agent for the United States."

The lower court held that the parties in the two actions are the same "since the Federal Reserve Bank was acting merely as the fiscal agent of the United States."

While holding, in its Memorandum, that the Federal Reserve Bank was clothed with sovereign immunity from suit, the court below did not dismiss this action on the ground that it was a suit against the sovereign without its consent.

The Affirmance by the Court of Appeals.

The Court of Appeals affirmed the decision of the District Court holding that the authority of the Federal Reserve Bank of Atlanta to guarantee the payment of 90% of the balance of the indebtedness and to release the security given to the banks by the principal obligor, Country Club Village Corporation, was conferred by paragraph 3 of Executive Order No. 9112 which, it said, was ratified by Sec. 7 of 56 Stat. 351, enacted June 11, 1942.

ARGUMENT.

The Applicable State Law.

The contracts of pledge were made, executed, and to be performed in the state of Alabama, and the rights of the parties were governed by the law of that state. **Hiscock v. Varick Bank, 206 U. S. 28, 27 S. Ct. 681, 51 L. ed. 945.**

It is a settled rule in Alabama that a mortgagee who has exercised a power to sell at a **private sale** is chargeable in equity upon a bill for an accounting and redemption, with the reasonable value of the property sold, regardless of the price actually received. **De Moville v. Merchants & Farmers Bank, 237 Ala. 186 So. 704, 713; Murphy v. Merchants National Bank of Mobile, 240 Ala. 688, 200 So. 895, 904; Marsh et al. v. Elba Bank & Trust Co., 221 Ala. 683, 130 So. 323; Zadek v. Burnett, 176 Ala. 80, 57 So. 47, 450; Johnson v. Selden, 140 Ala. 418, 37 So. 249, 103 Am. St. R. 49. Harmon v. Dothan Nat. Bank, 186 Ala. 360, 64 So. 621.**

In **Mahone v. Williams, 39 Ala. 202, 217,** the Alabama Supreme Court declared:

> "It is the primary duty of one charged with making a sale, to adopt the mode which will probably command the best price, and to exercise his best judgment in determining what is the mode likely to accomplish that end; and a sale in a manner variant from that which was known to be most likely to produce the largest price, would be sufficient reason for avoiding the sale. So, also, a failure to sell in the mode which a reasonable exercise of the seller's judgment would have shown to be the most probable means of bringing the largest price, would be a good ground of objection to a sale, where the price is altogether inadequate."

Where the lands are in "separate parcels, distinctly marked for separate and distinct enjoyment," there is a "reasonable presumption, sanctioned by observation and experience, that such property will produce more when sold in parcels than en masse, because the sale is thus accommodated to the probable wants of the purchasers." **Dozier v. Farrior, 187 Ala. 181, 65 So. 364.**

In **Bank of New Brockton v. Dunnavant, 204 Ala. 636, 87 So. 105,** the Alabama Supreme Court said:

> "Somerville, J. The Allegations of the bill present two distinct theories upon which the right of redemption is grounded: (1) That the foreclosure sale under the power is voidable at the instance of the mortgagee because the two farms, which are separate and distinct in location, equipment, and use, were sold en masse, which was highly disadvantageous and injurious to the mortgagor; that the mortgagee was the only bidder; and that the price of $5,517.45, which was bid and paid for the entire property, was grossly disproportionate to its real value, which was not less than $20,000; and (2) . . . In a court of law a power of sale is merely part of a legal contract to be executed according to its terms. In a court of equity it is quickened with the elements of a trust, and the donee of the power is charged as a quasi trustee with the duty of fairness and good faith in its execution, to the end that the mortgagor's property may be disposed of to his pecuniary advantage in the satisfaction of his debt." Harmon v. Dothan Nat. Bk., 186 Ala. 360, 369, 64 South 621, 624. To the same effect is Dozier v. Farrior, 187 Ala. 181, 65 South. 365, cited in note, L. R. A. 1917B, 527, 528.
>
> In Dozier v. Farrior, supra, it was held that a sale, under the power of widely separated tracts,

devoted to separate and distinct uses, made en masse, and bringing for the property a price greatly less than its real value, would be set aside in equity, letting the mortgagor in to redeem. In this aspect of the bill its allegations are sufficient to authorize the relief prayed, and the demurrer was properly overruled. We do not overlook respondent's contention that the mortgagee's equitable duty in the premises was abrogated by that provision of the power which authorized a sale "when, as, and where it shall seem best to them, for cash or on credit." A court of equity, however, will not allow the mere latitude of the mortgagee's discretion—a specific mode not being prescribed—to nullify a duty enjoined by law as essential to the ends of justice, and constituent in the obligations of a trust. As said by the Supreme Court of Illinois in a similar case:

"The power given, by its very terms, implies that the trustee assumed the duty of thinking on the subject, and that he should adopt that course which he should think would secure a good price. It does not mean that the trustee may do as he may please, or that he may do that which should be the most convenient for him." Cassidy v. Cook, 99 Ill. 385, 388.

In **Johnson v. Selden, 140 Ala. 418, 37 So. 249, 103 Am. St. R. 49,** it was held that the sale of property in lump or en masse was in itself prima facie evidence of unfairness. The Alabama Supreme Court stated:

". . . Here the property, which consisted of different items, such as mules, wagon, carriage, and farm products, was sold en masse, or in lump. This, in itself, was prima facie evidence of unfairness: Jones on Chattel Mortgages, 4th ed., p. 781, Sec. 797. The question of value was one for the jury."

See Annotation: Amount of Property Sold Under Mortgage Foreclosure in **L. R. A. (N. S.), 1917B, pages 517, 526-7.**

Petitioners (plaintiffs below) in their complaint alleged:

13. Plaintiffs further aver that the defendant participated in making the sale of the assets and property held by the pledgees for the security of the indebtedness of the Village Corporation resulting in a wanton sacrifice of the security and property. After the sale to Spring Hill Homes, Inc., for only $37,140.00, the purchaser, according to the records of Mobile County, Alabama, sold off the individual houses for amounts sufficiently above the amounts of the F. H. A. insured first mortgages to realize profits as follows:

For the period ending 12/31/45	$ 19,387.28
1/1/46 to 8/16/46	157,350.85
8/16/46 to 12/31/46	73,345.78
1/1/47 to 8/16/47	56,553.65
8/16/47 to 12/31/47	61,585.45
In the calendar year 1948	10,615.55
1949 through 1957	4,950.00
Total	$383,988.56

Said sale was not made in good faith but was fraudulently contrived by the banks and the defendant to give the property to one favored by them (for undisclosed reasons) at a fraction of its value and so as to extinguish the statutory right or redemption of two years under the laws of Alabama, which was a valuable right belonging to the Village Corporation, the original mortgagor (and consequently, to plaintiffs who were the equitable owners of the property, according to the laws of Alabama.)

14. . . . Plaintiffs aver that had the defendant and the banks exercised ordinary good judgment in the management of the security by collecting the rentals therefrom and by complying with the laws of Alabama, the entire indebtedness would have been paid in full. The estimated value of the houses and improvements, according to Federal Housing Administration appraisals, was in excess of the amount of the banks' indebtedness and the purchaser of the subdivision, as has been shown, realized a profit far in excess of the F. H. A. estimated values.

"15. Plaintiffs aver that the defendant as pledgee succeeding to the duties in part of the two banks occupied a fiduciary or trust relationship towards the plaintiffs and was under a duty to manage the security and property of the Village Corporation for the best interests of the plaintiffs as well as the United States of America. . . .

. . . . . .

Wherefore, plaintiffs demand:

a) Judgment against the defendant for the value of their stock in Country Club Village Corporation at the time of the sale of the subdivision property to Spring Hill Homes, Inc., less the amount received from said purchaser, together with interest from the date of said sale to Spring Hill Homes, Inc.; and all costs of the action.

b) All such further and general relief as is just."

The banks through their control of the corporation holding the title sold all 413 houses subject to the F. H. A. guaranteed mortgages on the individual houses at a private sale without notice to the guarantors, Hart and Russell, and, without any notice to the public. A specific mode of realization upon the pledge was not prescribed. The banks and the federal reserve bank evidently pre-

sumed from the want of any such specification, that they could deal with the subdivision property as they pleased. But, if so, they were laboring under a very serious mistake or misconception as to the law of Alabama. For, in **Bank of Brockton v. Dunnavant**, *supra*, the provision of the power which authorized the sale, "when, as, and where it shall deem best for them, for cash or on credit," was about as broad as the mind can conceive. The Alabama Supreme Court, however, held that a court of equity will not allow there mere latitude of the mortgagee's discretion—a specific mode not being prescribed—to nullify a duty enjoined by law as essential to the ends of justice, and constituent in the obligations of the trust.

The law declared by the Alabama Supreme Court in **Bank of Brockton v. Dunnavant**, *supra*, is, of course, hornbook law. In **Pauly v. Trust Co., 165 U. S. 606 at page 620, 17 S. Ct. 465, at page 470, 41 L. ed. 844**, Mr. Justice Harlan said:

> "That the pledgee of personal property occupies towards the pledgor somewhat of a fiduciary relation, by virtue of which, he being a trustee to sell, it becomes his duty to exercise his right of sale for the benefit of the pledgor."

Dibert v. Wernicke (C. A. 6th), 214 Fed. 673, lays down the rule that a mere literal compliance by the pledgee with the terms of the pledge, was not sufficient to render valid its sale and purchase of the pledged property.

Clearly, the allegations in the complaint in the case at bar that the federal reserve bank and the two Alabama banks, through their dummy directors and officers of the Realty Corporation, made a private sale of the **entire subdivision** to a man named Ellinor for $37,140.00, allowing him to give a check against uncollected funds, that after the sale (on October 2, 1945) the purchaser (Spring Hill Homes, Inc.) sold off the individual houses for amounts

sufficiently above the amounts of the F. H. A. insured first mortgages to realize profits of $19,387.28 for the period ending Dec. 31, 1945 and $157,350.85 for the period from Jan. 1, 1946 to Aug. 16, 1946 by Alabama law state a cause of action for breach of the fiduciary duty of fairness and good faith in the execution of the power conferred by the pledge agreement to the end that the property be disposed of to the pecuniary advantage of Country Club Village Corporation and Hart and Russell, the guarantors of its indebtedness.

By Alabama law, as has been shown, the mere fact that the sale of the subdivision was in lump or en masse is prima facie evidence of unfairness.

Former Judgment No Bar.

The Court of Appeals in its opinion said that the district court held that all but one of the specific issues raised by the complaint had been decided in the prior case and the doctrine of collateral estoppel was applicable.

Petitioners would show to the Court that the Court of Appeals in the prior case decided merely that the evidence adduced by the defendants Hart and Russell of offers by other parties to purchase the entire subdivision in lump or en masse did not rebut the prima facie case made by the certificate of indebtedness of the General Accounting Office showing the balance of indebtedness owing and that they did not carry the burden of "substantially proving" the defense of bad faith dealings on the part of the banks "with the government's assent." The point that by the law of Alabama the sale of the entire 413 houses in lump or en masse was prima facie evidence of unfairness, was not raised in the former case.

In **DeSollar v. Hanscome, 158 U. S. 216, 221, 15 S. Ct. 816, 39 L. ed. 956,** it was declared:

"Now it is of the essence of estoppel by judgment that it is certain that the precise fact was determined by the former judgment."

Does the judgment in the former case that the defendants failed to carry the burden of "substantially proving" the defense of bad faith dealings on the part of the banks negative the facts upon which petitioners base their cause of action against the federal reserve bank—a different cause of action from the suit by the United States on the note?

In **Owensboro v. Cumberland Tel. & Tel. Co., 230 U. S. 76, 33 S. Ct. 995, 57 L. ed. 1398,** this Court stated:

"The litigation, though between the same parties, is upon an entirely different cause of action. The bar of the former judgment is therefore confined to the questions which were actually litigated and decided in the former case, and it devolved upon the city to show in support of its plea, the cause of action being different in the present case, that the point here in issue was adjudged in the former case. DeSollar v. Hanscome, 158 U. S. 216, 39 L. ed. 956, 15 St. Ct. 816; Virginia-Carolina Chemical Co. v. Kirven, 215 U. S. 252, 54 L. ed. 179, 30 S. Ct. Rep. 78."

The district court did not find that the prima facie evidence of unfairness arising from the fact of the private sale of the entire subdivision in lump or en masse was rebutted by any **evidence.** Yet, under the rule stated in **Owensboro v. Cumberland Tel. & Tel. Co.,** *supra,* it devolved upon the federal reserve bank to show that this prima facie evidence of unfairness was satisfactorily rebutted. Otherwise the plea of former adjudication was not supported. It could not be aided by any presumption or argument from the former judgment. There was no presumption that the federal reserve bank and the two Alabama banks properly performed the duty of thinking

on the subject of what manner of sale would secure the best price and deemed that it was for the best interest of all parties concerned, i. e., the banks, the United States and the individual guarantors, Hart and Russell, to sell to Ellinor for a mere fraction of the value of the subdivision as estimated by Federal Housing Administration, but a short time before.

If any presumption could be drawn from the facts, it is one that is highly unfavorable to the defendant federal reserve bank. In neither the prior suit, nor in the case at bar, was any evidence produced by the government or by the federal reserve bank to show the reasons which impelled the private sale in lump or en masse.

Certainly, the federal reserve bank is not in position to insist upon a presumption that it performed its duty because it has, through the Justice Department, successfully avoided answering interrogatories propounded by petitioners in both suits directed to this precise point of the reasons which caused it to sacrifice the property. In the prior suit, Hart and Russell propounded interrogatories to the government, one of which was:

> "**Interrogatory No. 9.**—State specifically whether or not there were at least 400 houses in the Country Club Village, each having a fair value of from $1,000.00 to $1,200.00 in excess of the mortgage on each house and that said houses were sold for at least this amount by the said Ellinor within a short period of time after the property was conveyed to him and whether or not any accounting of profits was required by the said Ellinor."

The answer to this interrogatory signed by an assistant district attorney admitted that there were 413 homes in the project, but stated that "Plaintiff (United States of America) had no knowledge of their market value, or of the other matter inquired of in this interrogatory".

In the present action, petitioners propounded interrogatories to the then Attorney General of the United States, calling upon him to make an examination of the files of the War Department and Federal Reserve Bank of Atlanta

> ". . . and state your conclusion whether or not said sale was made in good faith, for a full, adequate and fair consideration and in the best interests of the United States of America, giving reasons for your conclusion."

Upon ex parte application of the United States District Attorney, the district court extended the time for objecting and/or answering the interrogatories until ten days after the ruling of the court on the defenses raised by the district attorney (appearing presumably under the direction of the Attorney General) in the motion for a summary judgment.

By other interrogatories filed in the present action, petitioners called on the federal reserve bank for the following information:

> "**Interrogatory No. 1.**—Please file and make available for inspection and copying all reports, communications, memoranda, letters, appraisals, documents and other writings in any way pertaining to the sale of the Country Club Village property to Spring Hill Homes, Inc., or L. B. Ellinor; or at your election, attach photocopies of same to your answer hereto.
>
> **Answer:**
>
> **Interrogatory No. 2.**—Is Mr. V. K. Bowman still connected with Federal Reserve Bank of Atlanta? If not, please give his address.
>
> **Answer:**
>
> **Interrogatory No. 3.**—Do you have among your papers and files, a copy of any report or appraisal of

Country Club Village Subdivision made by Federal Housing Administration? If so, please attach a copy thereof to your answer.

Answer:

.....

Attorney for Plaintiffs."

The interrogatories were never answered, for the reason that on ex parte application of the United States Attorney, the district court ordered that the time allowed to the federal reserve bank by Rule 33 of the Federal Rules of Civil Procedure to object or answer be extended to 30 days after the court shall have ruled on the validity of the affirmative defenses raised by the defendant federal reserve bank in its answer.

Petitioners, prior to the ruling of the district court sustaining the motion of the federal reserve bank for a summary judgment, moved to vacate the orders staying the discovery sought by their interrogatories upon the ground that they verily believed that the discovery sought would show that the defense of res judicata was not available to the defendant but this motion, too, was denied by the district court.

In **Cosby v. Buchanan, 23 Wall. 420, 23 L. Ed. 138,** this Court said:

> "Honesty of purpose prompts frankness of statement. Concealment is indicative of fraud."

In **The New York, 3 Wheat. 59, 4 L. Ed. 33,** it was held that the failure of one who has committed an act which unexplained is a violation of law, to bring forward material evidence which is in his possession of witnesses who are in his power and who are acquainted with all the circumstances of the case, is ground of suspicion and distrust. Cf. **Mammoth Oil Co. v. U. S., 275 U. S. 13, 48 S. Ct. 1, 72 L. ed. 137.**

It will be noted that the Court of Appeals, in its opinion, did not make a finding of its own that all of the issues raised by the complaint had been decided by its judgment and opinion in the prior case. It merely said that the district court, in its opinion held that all issues had been decided and that the doctrine of collateral estoppel was applicable. Neither court below could point out any evidence in the record of the prior suit or the present one which so much as tends to show that the banks and the federal reserve bank, after taking due care and thinking upon the subject of how to realize the most from the 413 houses in the subdivision to pay the balance of the indebtedness owing to the United States 90% and the two Alabama banks a mere 10%, and for Hart and Russell, too, made an honest and good faith decision that it was best to sell the property privately in lump to Ellinor or Spring Hill Homes, Inc.

After staying the answer to all of the plaintiffs' interrogatories that would have revealed the facts about the sale and the reasons why the subdivision was sold in lump, the district court, in its memorandum, said:

> ". . . It is clear from the agreement that a broad discretion is vested in the banks (assignors of Federal Reserve) with reference to enforcement of collateral and as to questions of sale and foreclosure, and the allegation that Federal Reserve during this period prevented sales to individual home owners, standing alone, and in the context of the facts as they existed, amounts to nothing more than a decision made by the Bank in the proper exercise of discretion, not to continue after default in liquidating collateral to sell lots separately but to sell all of the remaining real estate as a whole."

As petitioners have shown, the rule in Alabama is that *prima facie* the decision not to sell the lots separately

was an improper exercise of discretion by the federal reserve bank. This prima facie case could only be rebutted by evidence.

Petitioners, therefore, say that the former judgment is not conclusive of the question of the validity of the sale of the subdivision. All that was decided was that Hart and Russell did not carry the burden of "substantially proving" that the sale price of $37,100.00 was not the reasonable value of the property, and that the legal presumption. According to the law of Alabama, of unfairness of the sale arising from the fact that the 413 houses were sold privately in lump is unrebutted by any evidence in the record in the two cases. Therefore, the precise point in issue was not adjudged in the former case and the issue of the fairness of the sale remains at large for determination on evidence in the present case.

Actions of Federal Reserve Bank Unauthorized by Law—Privity With United States of America Lacking.

Another reason why the federal reserve bank is not entitled to invoke the judgment in the prior suit in which the United States of America sued the guarantors, Hart and Russell, is that it does not stand in any privity relationship with the United States.

In **Case of Tweed, 16 Wall. 504, 21 L. Ed. 389,** this Court declared:

> "Whenever a person sued sets up a defense that he was an officer of the government acting under color of law, it plainly devolves upon him to show that the law he invokes authorized the act in question to be done, and that he acted in good faith; . . ."

The Court of Appeals held that paragraph 3 of Executive Order No. 9112 authorized the Federal Reserve Bank

of Atlanta "to take such action as it did and of which complaint is made herein." Complaint is made first that the federal reserve bank was not authorized to execute the guarantee agreement as fiscal agent of the United States of America on behalf of the War Department.

The purpose of Executive order No. 9112 of March 26, 1942 was to authorize the War and Navy Departments and the Maritime Commission to guarantee loans to provide working capital for armament contractors and subcontractors. No authority was conferred upon these three agencies or departments to guarantee loans for housing. Executive Order No. 9070 of February 24, 1942 had consolidated the housing agencies and functions of the Government into the National Housing Agency.

As stated in the Guarantee Agreement executed by the federal reserve bank, the loan made by the two Alabama banks to Country Club Village Corporation was for the following purposes:

> ". . . to finance Borrower in the construction of 425 single family dwelling units with other improvements, including streets, water distribution systems, and power lines; said dwelling units to be located on a tract of land situate in Mobile County, Alabama, on Old Shell Road near Springhill."

The only authority which any agency of the government had to guarantee a loan for such purpose was that conferred by the National Housing Act Amendment, Ch. 319, 77th Cong., 2d Sess., Approved May 26, 1942—56 Stat. 301 authorizing the Federal Housing Administrator to insure mortgages on property designed for rent for residential use by war workers where the principal obligation did not exceed $5,000,000.00 or 90 per centum of the amount which the Administrator estimated would be the reasonable replacement cost of the completed property or project.

The Court of Appeals did not state **expressly** that Executive Order No. 9112 conferred authority upon the War Department to guarantee loans for housing, such as the one made by the two banks to Country Club Village Corporation. It said that Sec. 7 of 56 Stat. 351, approved June 11, 1942, ratified "the grant of authority given the War Department under this executive order." This, of course, left undecided the question—if any question could reasonably be said to exist—as to what actually was the grant of authority to the War Department by Executive Order No. 9112.

A mere perusal of Sec. 7 of 56 Stat. 351 approved June 11, 1942 (the Mobilization of Small Business Act) makes it clear beyond the peradventure of doubt that Congress well understood that the purpose of Executive Order No. 9112 was to authorize the three agencies named therein to guarantee loans made pursuant to the Mobilization of Small Business Act "with a view to increasing the production of war materials, supplies, or equipment." Congress by Section 7 of the Act further authorized the agencies to use any funds "heretofore or hereafter made available to them for purposes of procuring war materials, supplies, and equipment, or of expediting the production thereof."

There is no mention of defense housing in either Executive Order No. 9112 or the Mobilization of Small Business Act. The authority for insuring loans for defense housing was conferred upon the Federal Housing Administrator by other legislation and Executive Order No. 9070.

The Board of Governors of the Federal Reserve System on April 10, 1942 announced the adoption or Regulation V to carry out the President's Executive Order No. 9112 of March 26, 1942, for the purpose of facilitating and expediting the financing of war production. In a statement for the Press, the Board of Governors stated that the

regulation was adopted after consultation with the War Department, the Navy Department, and the United States Maritime Commission and said:

> "Under the Executive Order the three military procurement agencies are authorized to guarantee commercial banks, Federal Reserve Banks, the Reconstruction Finance Corporation, or other financial institutions **against loss on loans made to concerns to finance the performance of war orders**..." (Emphasis added).

Federal Reserve Bulletin, May 1942, pages 424-427.

Nothing could be plainer than that the only authority for guaranteeing loans for defense housing was that conferred by the Amendments to the National Housing Act and that Congress did not intend to confer authority upon the War Department to guarantee such loans. The liaison officer of the War Department stationed at the Federal Reserve Bank of Atlanta who signed the Statement of Necessity for the guarantee of the loan to Country Club Village Corporation of course, did not have the power to authorize Federal Reserve Bank of Atlanta to disregard the laws enacted by the Congress.

Want of Authority in Federal Reserve Bank of Atlanta to Release Lien to Allow Private Sale of Subdivision to be Made.

As Executive Order No. 9112 conferred no authority on the federal reserve bank to act as fiscal agent of the United States executing on behalf of the War Department a guarantee of a loan for residential housing, even though it be called "defense housing", it could not furnish the basis for an **implied** power to receive and enforce any rights to collateral securing such an unauthorized loan. Yet, par. 3 of Executive Order No. 9112 was cited by the Court of

Appeals as authorizing the federal reserve bank "to take such action as it did."

Petitioners do not deem it necessary to cite the numerous decisions of this Court upholding and enforcing the rule that the powers of governmental representatives are created, defined and limited by legislation and no act by an agent exceeding his legislatively delegated authority constrains the United States. Even if the federal reserve bank were an officer of the government acting under color of law—and we have shown that neither proposition is sustainable in the case now before the Court—in this action by individuals for injury occasioned by its acts, according to the rule declared in **Case of Tweed**, *supra*, it plainly devolves upon it to show that the law it invokes authorized the release of the lien upon the subdivision to allow the private sale to be made. This has not been done in the case at bar.

In **American Sales Corporation v. United States (C. A. 5th), 32 F. 2d 141**, affirming **U. S. v. American Sales Corporation, 27 F. 2d 389**, and cer. den. **American Sales Corporation v. U. S., 280 U. S. 574, 50 S. Ct. 29, 74 L. ed. 625**, the statutes were held to empower the Secretary of War to contract for the sale of surplus war materials, retaining in the government possession and title until the price was paid. But, it was held that where the Secretary made such contracts which were partly executed, he was without authority to release rights vested in the government by those contracts by reducing the contract price. The authority to make the original contracts, the court said, did not imply authority to cancel them or to relinquish rights thereby acquired.

Doctrine of Sovereign Immunity Not Available to Federal Reserve Bank.

The federal reserve bank, of course, is not an officer or agency of the United States. Even Federal agencies or instrumentalities do not acquire the government's immunity from suit merely because they do its work. **Keifer v. R. F. A., 306 U. S. 381, 59 S. Ct. 516, 83 L. ed. 784.** The power to grant or withhold immunity from suit on behalf of a government corporation is in Congress. **Brady v. Roosevelt S. S. Co., 318 U. S. 575, 63 S. Ct. 425, 87 L. ed. 471.**

Assuming that Congress would have had the power to grant immunity to federal reserve banks for any action taken pursuant to Executive Order No. 9112, it did not do so by the "Act for the Mobilization of Small Business for War Production" or any other statute. If what was done was within the authority conferred upon the War Department by Sec. 7 of the Act, the Federal Reserve Bank would have been under no liability anyway, because there is no liability on the part of a public officer for executing the will of Congress.

We cannot assume that Congress would pass a law limiting the authority of an agency to do certain things and, by the same act, undertake to confer an unlimited immunity against any liability for acts done in excess of the authority granted and even for fraud. Neither can we assume that the President, whose authority is limited to enforcement of the laws enacted by the Congress, not to making them, would presume to grant an immunity from liability for acts done in excess of authority and in fraud upon the United States and third persons. An overtowering public policy which makes an agent liable for for his own negligence or fraud has been so long embedded in the law as to forbid such a construction of Executive Order No. 9112.

Surely, it would be unsound reasoning to hold that Federal Reserve Bank was carrying out its proper functions because the President, by the executive order, directed that in guaranteeing loans as agents of the War Department, the federal reserve banks would be exempt from personal liability even though the loans were outside the scope of any authority conferred upon the War Department. That an attempted grant of immunity from liability should operate as a grant of authority contrary to the expressed will of the Congress would be a novel doctrine.

The only reasonable interpretation that can be given the exemption from liability clause in the executive order is that federal reserve banks executing guaranties as agent for the three agencies named in the order were not to be personally liable for payment to the obligees. To construe the provision otherwise would be to hold that the President intended to circumvent the will of the Congress and assume law-making authority to set aside an ancient and time honored rule of law and fundamental public policy.

For the reasons shown, Par. 3 of Executive Order No. 9112 does not operate to clothe the Federal Reserve Bank of Atlanta with the immunity of the sovereign for the acts done by which complaint is made herein.

It has been shown that the implication in the opinion of the district court which the Court of Appeals expressly approved that the federal reserve bank was "carrying out its proper functions in complying with its statutory obligation as an insurer of 90% of the Hart and Russell indebtedness, and in receiving and enforcing all rights to collateral security after payment" is without foundation or warrant in law.

Since what was done by the Federal Reserve Bank was not within the authority validly conferred by the Congress, it is responsible to the full extent of the injury caused thereby. **Herd & Co. v. Krawill Machinery Corp., 359**

U. S. 297, 3 L. ed. 2d 820, 79 S. Ct. 766; Brady v. Roosevelt S. S. Co., 317 U. S. 575, 63 S. Ct. 425, 87 L. ed. 471; Sloan Shipyards Corp. v. United States S. Bd. E. F. Corp., 258 U. S. 549, 567, 66 L. ed. 762, 42 S. Ct. 386. Petitioners should be given the opportunity to prove the allegations of fraud. If the Federal Reserve Bank acted fraudulently, as alleged, it would be liable in damages to them and the United States. **Lee v. Monroe and Thornton, 11 U. S. 366, 3 L. ed. 373.**

REASON RELIED ON FOR GRANTING THE WRIT.

In holding that the Federal Reserve Bank of Atlanta was clothed with the immunity of the sovereign from liability for acts which by applicable state law were in flagrant violation of the duty of a fiduciary and by rulings barring any investigation of its conduct, the courts below have nullified the public policy requiring strict accountability of every agency or agent handling public funds and property and the rule declared by this Court in **Case of Tweed** imposing upon one claiming to act as an officer of the government under color of law the duty of showing that he acted in good faith.

PRAYER.

Wherefore, petitioners pray that a writ of certiorari issue from the Honorable Court; and that the judgment dismissing this action be reversed and the case remanded for trial in the district court according to the usual course of such proceeding.

This October 18, 1967.

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